

## Loans for Businesses Vital Goal of Stimulus

We have all heard about the Economic Stimulus package that is going into effect this year. It is hard to think about the government just printing up so many dollars and the continuing incline to our national debt, but getting those dollars turning over in the economy is very powerful. As I mentioned in last October's article, the turnover of dollars is what creates jobs whether that job be for scientists, engineers, contractors, store clerks or farmers. We are all dependent on each other to make money and to spend money for our economy to thrive.

Part of the Economic Stimulus package is targeted towards helping small business through the programs offered by the U.S. Small Business Administration (SBA), primarily the guaranteed loan programs. As many of you have experienced during the past year, the banks have not been as willing to lend money. Without the opportunity to borrow, small business has found it even harder to place themselves in a position that helps them

weather the storm brought on by this recession.

The Stimulus package will, hopefully, create the opportunity for lenders to get back into making loans through three primary provisions. The first is to re-open the secondary market, the second is to raise guaranty levels and the third is to reduce loan fees. To understand how this will help your business get the financing you need, let's review how the SBA guaranteed loans work.

First of all, it is important to understand that the SBA does not loan directly to individuals. They guaranty loans through financial institutions. Locally, we have many lenders that offer SBA guaranteed loans.

**U.S. Small Business Administration**



Financial institutions are businesses, the same as everyone else. They are looking to earn revenues and be profitable. The way they earn revenues is to lend money. However, lending

money to business is very risky. Just think about how much interest a bank has to earn on many loans in order to cover the default of just one loan. The banks, on their own, would only loan to very low-risk businesses, generally those well established businesses that have outstanding credentials.

But the U.S. government knows that small business is the strength of America and wants to make it possible for small business to get the financing that it needs. To do this, they guarantee a portion of the loan with the financial institution. Then when a business defaults, the government steps in and pays the bank the portion guaranteed, reducing the loss to the financial institution. (Of course, the government at that point has taken a loss and is very interested in recovering from the guarantors of the loan.) As a result of this guaranty, the financial institutions will look to lend to businesses that may be rated medium-risk. Neither the financial institutions nor the SBA, through the guarantee, are

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willing to lend to high-risk businesses.

The SBA assesses a loan fee on the funds they guarantee that is generally passed on to the borrower. Depending on the loan, this fee may be as high as 3% of the guaranteed amount. This can be a substantial cost to the borrower, that adds to the cost of doing business.

The bank, then holds and collects on the loan. However, in order to maintain their FDIC rating, they can only carry a certain percentage of loans to total assets. So in order to continue making loans, they can sell, to a secondary market, the SBA guaranteed portion of the loans held in the books. The loans are sold to companies that pool them together and then turn around again and sell the pooled loans as securities to investors. Investors speculate on the return on investment on these pooled loans the same as for stocks and bonds. The bank makes a reduced return but is able to free up more monies to continue making loans.

During the recent collapse of the stock market, investors were no longer interested in purchasing these pooled loans. That meant that the banks could no longer sell the loans locking up their ability to make new loans. And the dominoes tumbled down from there to our small businesses in towns and cities across the nation.

So back to the three provisions included in the Stimulus package. First, the U.S. Treasury Department will buy up the securities of pooled loans on the secondary market, opening up the ability for the banks to start lending again. Second, the SBA will be able to guarantee up to 90% of the loan, reducing the risk to the banker even more. And finally, the temporary elimination of certain loan fees will reduce the cost to the borrower of taking out the loan. This has all the key elements needed to get loan funds flowing again.

The increased guaranty amount and the eliminated loan fees are already in effect. The SBA is still working on the regs and policies for purchasing the

loans on the secondary market; we hope to see it take effect in the near future. For even more details about how this plan may help your business, go to [www.sba.gov](http://www.sba.gov) and click on the "Economic Recovery" icon.

Lastly, it is also important to understand that there is no provision in the Stimulus package to give grants or tax rebates to small businesses. There are a lot of scams coming out of the woodwork. Do not, even if a letter includes a seemingly realistic letterhead from the Small Business Administration, provide bank account information to anyone unless you have initiated the contact. Do an Internet search on "economic stimulus scams" for more information.

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